OMB 123, Appendix A

Process of Preparing the Report on Internal Controls Over Financial Reporting

Mary Braun

Office of the Under Secretary of Defense (Comptroller)

Financial Improvement and Audit Readiness Directorate

PURPOSE

Appendix A (Dec 21, 2004):

- Issued under FMFIA of 1982
- Federal Government's response to SOX
- Provides new internal control standards
- Defines prescribed process for conducting assessment of internal control over financial reporting

Requirements

- Establish Senior Assessment Team
- Assess internal control at process, transaction, application levels
- Document internal controls
- Document assessment
- Assert effectiveness of internal control
- Develop corrective action plans

DoD SAT Requirements

- Establish a Senior Assessment Team to:
  - Determine material reports
  - Set materiality
  - Establish focus areas
  - Issue guidance
  - Report on internal controls
  - Monitor corrective action plans

DoD SAT Members

- DUSDs from focus areas
- DASDs from focus areas
- DUSDs from support areas (NII, Intel, Policy)
- IG, DoD
- Service FMs

Component Senior Assessment Team

- Senior Leadership determines membership
- Members determine material functions
- SAT members include representatives from material business lines who are
  - Decision making leaders
  - With:
    - functional expertise
    - resources for monitoring progress
    - buy-in to improvement
- Document, document, document

Senior Assessment Team
Responsibilities

SAT will:

- Follow DoD guidance for reporting categories
- Identify material business lines/processes
- Narrate and flowchart business process
- Identify assess risk
- Document internal controls
- Assess controls for design & application
- Report on effectiveness

Document, document, document

Senior Assessment Team

DoD SAT will:

- **Identify material lines**
- **Document, document, document**

CONSOLIDATED BALANCE SHEET		2005 Consolidated	Army GF	USACE	Air Force	Navy
Materiality threshold = .99 % Adj Assets		**14,082**	**14,082**	**14,082**	**14,082**	**14,082**
ASSETS (Note 2)						
Cash and Other Monetary Assets	$	2,165	1,571,490	1,094	147,468	289,290
Accounts Receivable (Note 5)		7,259	608,146	1,772,808	969,920	3,000,205
Inventory and Related Property		209,265	35,901,175	102,747	48,643,476	54,289,582
General Property, Plant and Equipme		447,610	114,541,559	26,990,299	119,949,046	155,226,068
Real Property		97,704	20,989,574	26,286,504	21,674,187	18,126,987
Military Equipment		324,440	9,243,000	0	90,240,000	136,600,000
Investments (Note 4)		503	0	0	0	0
Other Assets (Note 6)		24,711	3,488,672	0	11,535,139	7,637,554
TOTAL ASSETS	$	1,424,561	278,069,240	38,340,859	298,584,695	363,407,841

Identify Key Processes

- **Determine key processes which create material balances on financial reports:**

- **Include:**
  - **FBwT**
  - **Investments**
  - **Military Equipment**
  - **Real Property**
  - **FECA Liabilities**
  - **Environmental Liabilities**
  - **Appropriations Received**
  - **Accounts with material balances (i.e.; Gross Costs w. Public)**

- **What processes cause a balance increase? (Do you need to ask DFAS?)**

- **What processes cause a balance decrease?**

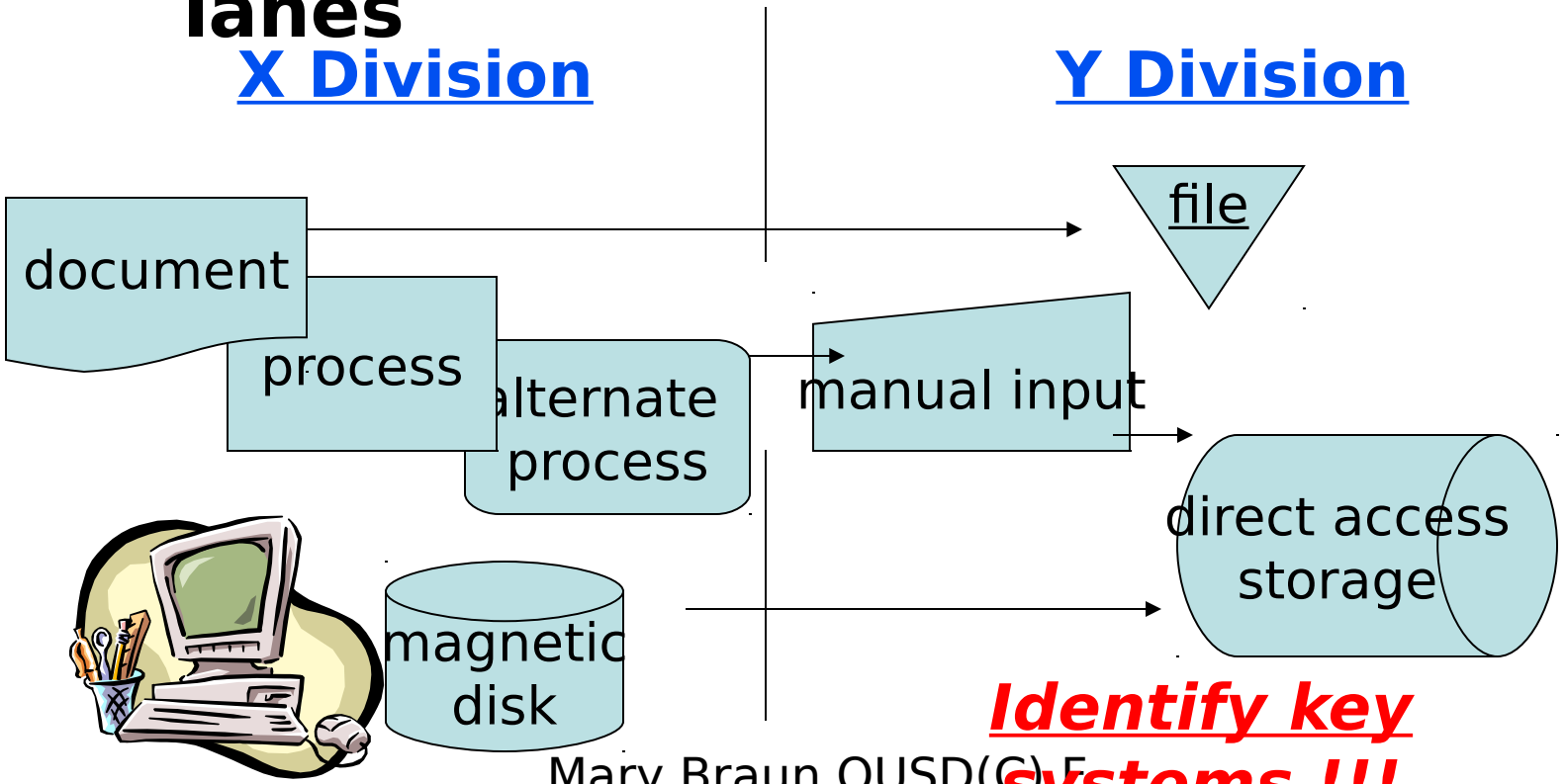
- **Document, document, document**

Narrate Process

- **Narrate the process**
  - **Trace transaction from point of origination through financial reports and back again**
  - **Will require participation of those with knowledge of bu processes/ transactio**

Flow Chart Process

- **Flow chart the process:**
  - **Use org chart for swim lanes**



Identify key systems !!!

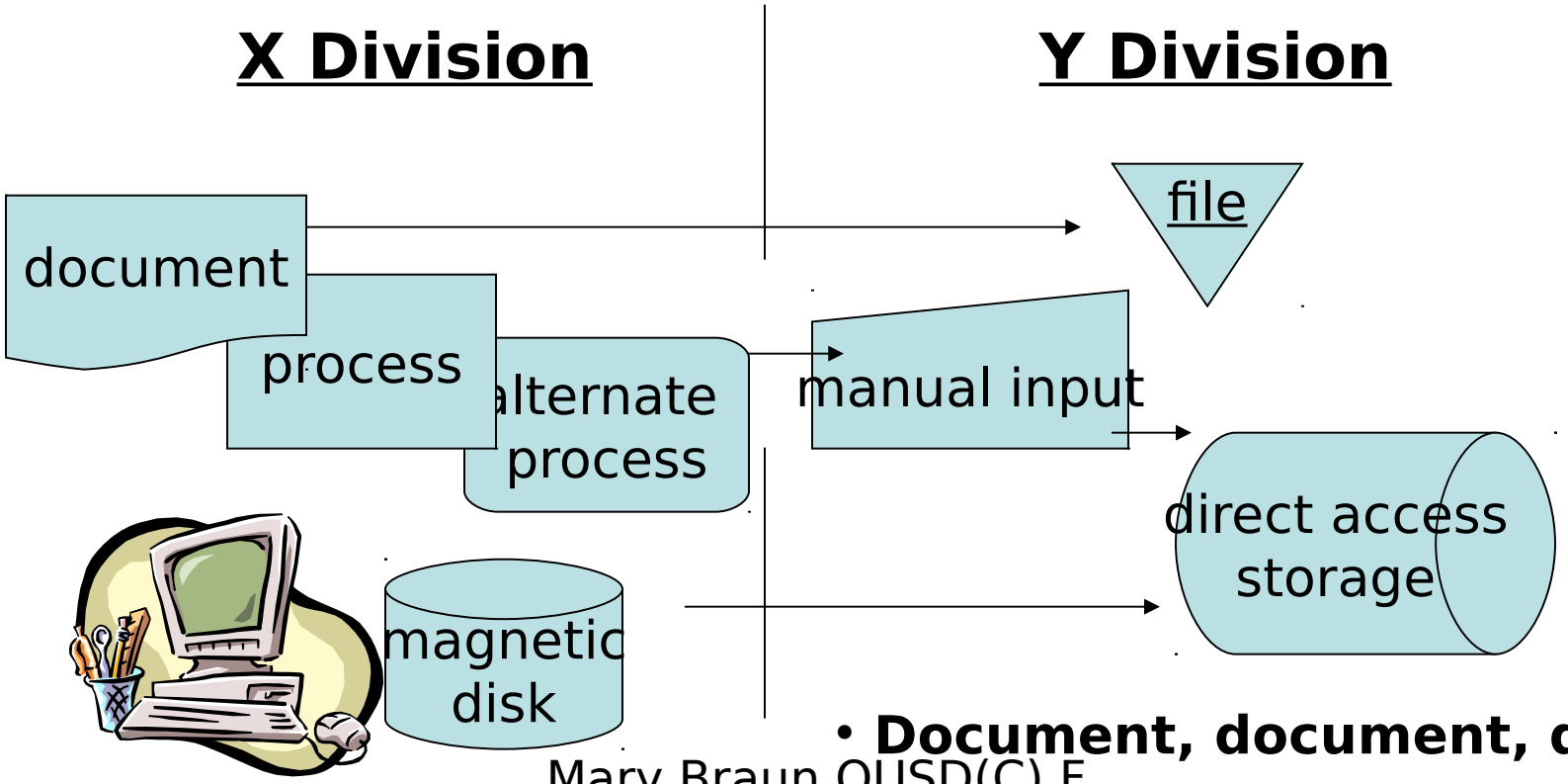
Management Assertions

- **Completeness**
- **Obligations/Rights**
- **Valuation**
- **Existence/Occurrence**
- **Reporting/Presentation**

Identify Risk Areas

Wherever there is a transfer, there is a risk!

What are the risks that an assertion might not be valid? Might be circumvented?



- **Document, document, docume**

Process: Assess Risk

Risk Assessment					
	Event	Event	Event	Event	Event
example:	Purchasing	Receiving	Vendor Maintenance	Invoice Processing	Disbursement
High Risk					
Complex programs/operations					
Complex transactions					
Use of accounting estimates					
Extensive manual processes/applications					
Decentralized accounting/reporting functions					
Changes in operating environment					
Significant personnel changes					
New/revamped information systems					
New programs/operations					
New technology					
Moderate Risk					
Amended laws/regulations					
New accounting standards					
Personnel constraints					
Centralized accounting/reporting functions					
Static operating environment					
Low Risk					
Simple operations/accounting transactions					
Low transaction volume					
Management's Risk Assessment					

Assess Risk Areas

Use forms on Comptroller's public web site.

Risk Analysis

Entity

Preparer

Account Line: **Fund Balance With Treasury**

Control Number	Account/ Line Item/Event	Business Cycle, Accounting Application	Assertion	Risk	Inherent Risk	Control Risk	Combined Risk	Internal Control Currently In Place	Internal Control Test Method Used

Document, document, document

Identify Internal Controls

Identify your key internal controls

- What internal controls are in place to mitigate your risk?
- What were they designed to do?
- Is the design effective?
- Are the internal controls operating effectively?

Yes = test No = fix

- Document, document, document

Process: Assess ICs

Test Controls:

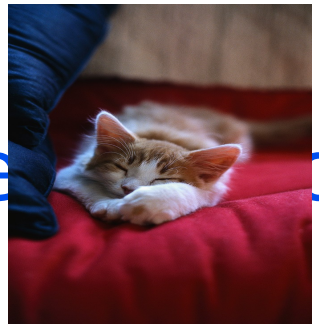
- **Design test plan**
  - **Interview**
  - **Observe**
  - **Inspect**
  - **Reperform**
- **Document plan**
- **Perform testing**
- **Document results**

Process: Identify Weaknesses

Management determines:

Materiality of weakness

- Reportable condition?
- Material weakness?



Material: affects
de of prudent person

Process: Correction Plans

- Develop corrective action plans for material weaknesses

  -- Prescribed format

  -- Enter in the DoD Financial Improvement web-based tool

- Document, document, document

Reporting Weaknesses

Management reports material weaknesses in the FIAR web-based tool:

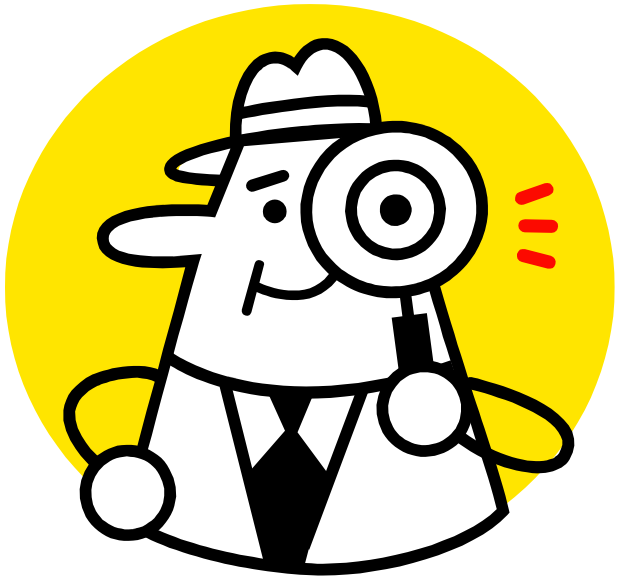
- Compo A reports weakness in SOA; Compo A corrects weakness
- Compo A reports weakness in SOA; Compo B reports and corrects weakness in SOA [A's attribute & B' attribute]
- Compo B corrects weakness and reports in SOA; Compo A reports weakness in SOA [B's attribute & A's attribute]
- Compo A reports weakness in SOA; Compo C corrects weakness (not in SOA) [A's & C's attribute]

Process: Report

- Report: Status and corrective action plans
  - Prescribed letter format
    - Unqualified
    - Qualified
    - No assurance
  - Tabs for discussion of weaknesses

Process: Monitor

- Monitor Corrective Action Plans:
  - SAT monitors at entity level and at DoD level
- Assure Progress
- Report on Progress



DoD Requirements

- Schedule of Deliverables:

What	When
Flow Charts	December 20, 2005
Risk Assessment	February 1, 2006
List of Controls	March 20, 2006
IC Evaluations	June 30, 2006
Corrective Action Plans	June 30, 2006

Guidance

- OMB Circular 123, Appendix A, as revised in 2004
- OMB Appendix A implementation guidance, released July 2005
- DoD guidance
  - Forms will be on Comptroller/FMFIA website
  - Provides examples
  - Web-based tool available on line
- DFAS flowcharts available at:

  https://Dfas4dod.dfas.mil/library/opr/

Consequences or Benefits?

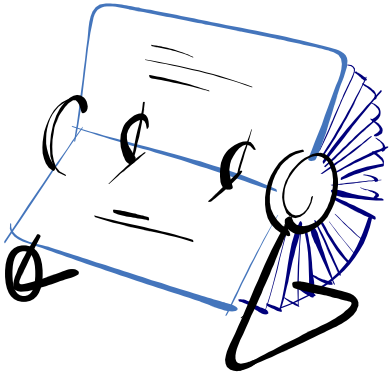
- You understand how business is really done and get to know lots of other people.
- Leadership wants to make improvements.
- Your internal controls ge
- You will be able to sustain your audit opinion easier.
- Audits will be easier.

Questions ???

CONTACT

Mary Braun

703-602-0300 x 120



mary.braun@osd.mil